

## MINUTES

BOARD OF TRUSTEES  
PUBLIC EMPLOYEES' RETIREMENT FUND  
143 West Market Street, Suite 602  
Indianapolis, IN 46204

June 1, 1998

### TRUSTEES PRESENT

Richard Doermer, Chair  
Nancy Turner, Vice Chair  
Dwayne Isaacs  
Dr. Teresa Ghilarducci  
Steven Miller

### OTHERS PRESENT

Diana Hamilton, Special Liaison to the Governor for Public Finance  
Doug Kinser, Executive Assistant to the Governor  
Mary Beth Braitman, Ice Miller Donadio & Ryan  
Dick Boggs, Burnley Associates  
Kris Ford, William M. Mercer Investment Consulting  
Pete Keliuotis, William M. Mercer Investment Consulting  
Victoria Yamasaki, Coopers & Lybrand  
Jackie Byers, Coopers & Lybrand  
Karen Franklin, National City Bank  
Faith Berning National City Bank  
Leland Tanner, Prime Capital Management  
Philip Barnes, Prime Capital Management  
Stephen Tufts, Prime Capital Management  
Garth Dickey, Immediate Past PERF Director  
Mark Webb, PERF Interim Director  
Patrick Lane, PERF Executive Assistant to the Director  
Bill Hutchinson, PERF Division Director, Pension Administration  
Michael Quigley, Program Director, Pension Administration  
Dave Yeater, PERF Controller  
Linda Petro, Recording Secretary

### ITEMS MAILED TO THE BOARD PRIOR TO MEETING

- A. Minutes of March 2 & 3, 1998 Meeting
- B. Statements of Retired and Disabled Members - PERF, Judges' Retirement System, Conservation & Excise, and Police & Fire
- C. Composite Portfolio Summary

- D. Quality Portfolio Statistics
- E. Historical Comparisons
- F. Balance Sheets - All Funds
- G. New Units & Enlargements

A quorum being present, Chairman Doermer called the meeting to order.

1. APPROVAL OF MINUTES

Following review by the Board,

**MOTION** duly made by Teresa Ghilarducci, seconded by Steve Miller and unanimously carried to approve the Minutes of the March 2 & 3, 1998 meeting.

2. COOPERS & LYBRAND REPORT

Victoria Yamasaki and Jackie Byers were present representing Coopers & Lybrand.

The Benefits Control Review Process (Phase 2) of the Coopers report has now been undertaken. Jackie Byers, who has been leading this portion of the project, noted that they had identified about 22 individuals and five employer groups with whom they have spoken. Among the 22 individuals interviewed were the Director, a number of key accounting staff, and several other accounting or benefits administration staff. In addition, they also interviewed a couple of individuals from the State Board of Accounts, the Special Liaison to the Governor for Public Finance, and the Budget Director. To supplement that they met with five employer groups of sizes representative of the different employer groups served by PERF. They also had some comprehensive meetings with some of the team leaders within the Benefits Administration area to try to get an overview of the processes related to the benefits cycle and how transactions flow.

Ms. Yamasaki noted that it is now important to collect these results and to meet with the newly-created Benefits Committee (staffed by two of the Board members) to start to formulate some findings and recommendations and then ultimately some action plans to address whatever findings come from the analysis of the interviews and process flow maps. Following their work with the Benefits Committee, they should have a report in order in time for the August Board meeting.

3. INVESTMENTS

Performance Analysis

Richard Boggs, Burnley Associates, reported that equity allocations during the calendar quarter January 1 to March 31 increased from 16% to 22%. The quarter was started with \$6.8 billion and ended with \$7.1 billion. There was \$12.5 million in net contributions with almost \$100 million in income. With stock markets up 14% and bonds up 1.6%, there was \$168 million in capital gains. If you look back to the beginning of 1995, the Fund had less than \$5 million and is now up to almost \$7-\$7.25. With the stock market being up 14%, assets changed from the end of December 1997 to the end of March 1998. During that time period, PERF put \$300 million in the market and gained approximately \$500 million in terms of commitment to the stock asset class. There was a 48% return in the equity index fund over the last 12 months. There wasn't much in the fund, but what was in it tied the index at 48%. The median manager was only up 44.4%.

Looking at individual manager performances, the index was up 1.6% and the range was very tight. A couple of managers were at 1.5% because they were short or they were overweighted in treasuries. A couple of managers were up at 1.8%.

The Fund has a corporate maximum of 60 percentage points, and Consecro was 57% in corporates and 12% asset backed securities. Asset backed securities are home equity loans which are primarily packaged by corporations, manufactured homes, trailers, and credit card receivables, for example. There is some dissension within the trade as to whether those are, in fact, corporate securities. They used to be a part of the Lehman Corporate Index, and then they were split out separately. So, the question arises as to whether Consecro was in violation of the 60% maximum with 57% and 12% equaling 69%. This was something that was brought up in length at the Board's Investment Committee meeting on May 28. After some discussion, there was a consensus of the two Board representatives and the other Investment Committee members to abolish the 60% maximum on corporates. The three managers interviewed this quarter (Consecro, Harris, and J. P. Morgan) all did very well. But when you look at where they were at asset backs, Consecro was 12%, Morgan was 14%, and Harris was 9%. They found the key to success is asset backs. In the new set of guidelines, the 60% maximum was included to keep someone from being 100% corporates. Consecro made the point, with a lot of validity, that part of the 12% are home equity loans and properly should be considered mortgages. Thus, the Investment Committee has recommended that the Investment Policy be amended to abolish the 60% maximum on corporates:

**MOTION** duly made by Steve Miller, seconded by Dwayne Isaacs and unanimously carried to amend the Investment Policy, page 24, as follows:

**! Core-Active Management**

Investment Constraints: Securities other than those which comprise the issuer and quality components of the index are

prohibited unless specifically approved by the Board. No portfolio may contain more than 40% mortgage securities, 60% corporate securities, or 10% securities rated BAA or BBB. No portfolio may vary in duration by more than 20% above or below the duration of the benchmark index.

Continuing with manager guideline violations, Harris holds some Korean Development Bonds which mature in the year 2004 and were downgraded below the Fund's minimum investment grade by two notches. They have since been upgraded one notch and can be held at the discretion of the manager. This has been discussed with Harris, and they feel that everything was an overreaction. They are continuing to hold them and feel they will be okay. They are allowed to do that under the PERF guidelines.

There is also a guideline feature which says that the duration shall be plus or minus 20%. HM Capital is marginally over 20% or more than 20% under. In discussing it with them, they have indicated that by their calculation they are right on the hundredth and that's where they intend to be. Thus, Mr. Boggs felt it necessary to bring the matter to the Board's attention and to note that it is costing a lot of points in performance.

There's no defense for it on their side except they guessed wrong. The only way HM adds value is by moving duration because they are 98% in treasuries. They keep looking for a surge in interest rates, and they sit patiently while the rates go down or stay the same. As long as that happens, they are going to lose performance. They could be in corporates, but they don't like corporates, asset backs, or anything other than what they are in which is shorter treasuries. It's hurting and hurting badly.

Following further Board discussion, it was determined that HM Capital should be scheduled to meet with the Board at its August meeting.

With respect to securities lending income, Bank One seems to be a much more efficient lender in terms of putting assets out on loan as a percentage of the allowable. The guidelines say 40% of the assets can be put out on loan, and of those 40%, Chase, over the last calendar year and over the March calendar quarter, put about 60-65% out on loan. Bank One was over 80%. In the cash collateral portfolio, PERF has 100% of the credit risk and gets 65% of the income. The securities lending people get 35% of the income. So various guidelines have been established to make sure that nothing is askew that could get the Fund into an embarrassing credit situation. The Fund bears all the credit risk, and the lenders get part of the income. An area in which a problem could arise is the corporate concentration. There is a 5% maximum per issuer. Chase had three issuers above 5% in the concentration. They have something called "STEERS" which is essentially a form of private placement home equity loan type paper all apparently put out by the same issuer. It has been

suggested to them that they not buy any more. They mature fairly quickly (within six months), and it was further suggested that they simply hold what they have until they mature. One of the reasons they have some issuers above 5% is that as bonds have been sold to put into the stock market, they have a shrinking lendable base and a shrinking cash collateral portfolio, so some of these were bought at cost and were less than 5%, but as monies are taken away they are more than 5%.

Looking at the split of securities lending as the Fund begins using a unit trust accounting system, the idea is that the securities lending be split roughly half and half between Bank One and Chase. The Investment Committee, at its May 28 meeting, did come to some agreement of giving Bank One their own Bank One portfolio and the Prime PERF-related, LBA Index Fund, and Reallocation Fund accounts and then adding to that the Brinson equity account, the Morgan equity account, and the Morgan small cap account.

**MOTION** duly made by Steve Miller, seconded by Teresa Ghilarducci and unanimously carried to split investment managers as recommended by the Investment Committee for purposes of securities lending.

Concerning cash flows, on March 31 there was a total of \$1.2 billion in the PERF-related account (all fixed income managed by Prime), \$5.5 billion in PERF fixed income, and \$1.6 billion in PERF equity. Then in April, \$100 million was moved from the fixed income portion over to the equity portion. The same was true in May. Now in June, the unit trust fund is being established. So all the Prime B (the old PERF-related fixed income fund) is starting out at \$1.2 billion which will be absorbed into everything that has been done in the PERF fund so far and done in such a way that everything is going to look the same by the end of the month. There is no money left in the Reallocation Fund, and money has to be pulled out of some active managers or the Index Fund in order to put money into equities. Mr. Boggs noted that he argued against taking it out of LBA Index Fund because the Index Fund does pretty well over long periods of time, and, as a rule of thumb, roughly half of PERF's money should be kept indexed in any asset class. Half of it should be kept indexed on the bond side as well. The bond index is currently under half, so it does not make sense to take money from there. There are two managers with \$800+ million. Whoever survives on the bond side will have maybe \$300 million each because there will be some diversification of managers. Thus, the thought is to give them \$300 million each. One of the ways of getting from here to there is to pull \$50 million per month out of First Chicago and the Prime A account (active account) which would provide \$100 million per month. Continuing to pull from First Chicago and Prime from their \$800+ level down to about \$300 would provide money until January/February of 1999. Such would provide that no managers would have to be terminated — the playing field would simply be leveled a little.

Also, the Prime B account (the old PERF-related) is currently 100% bonds. By the end of the month it should be down to roughly 75-76% bonds which is

where the rest of the PERF accounts are going to be. To get there from here would be to take \$300 million out and put it in equities. Thus, you would have the regular \$100 million transfer and a one-time \$300 million transfer to play catch up since these transfers have not been made in this account since May 1996 like was done in the regular PERF accounts. Going forward through July, \$50 million would continue to be taken each from First Chicago and Prime which would mean that the Prime B account would continue to lose \$20 million per month.

Following Board discussion,

**MOTION** duly made by Dwayne Isaacs, seconded by Steve Miller and unanimously carried to approve the June 1998 through July 1999 cash flow procedure as described.

With respect to third quarter contributions,

**MOTION** duly made by Steve Miller, seconded by Nancy Turner and unanimously carried to place third quarter contributions (in's and out's) into the Reallocation Fund.

#### Prime Capital Management

Leland Tanner, Philip Barnes, and Stephen Tufts were in attendance representing Prime Capital Management.

Mr. Tanner noted that during the first quarter of 1998 Prime shortened the duration of their portfolio to 4.81 years from 4.90 years. At that time they were still long on the benchmark of 107% of the index at the end of the quarter. They reduced their mortgage back holdings by 7% to 18% of the portfolio, and U. S. Treasuries were reduced by another 4% to 30% of the portfolio. These funded the addition of 9% to U. S. Agencies holdings during the quarter and 3% to industrial holdings. Their rate of return for the quarter was 1.63% as opposed to 1.54% for the LBA. Over six months Prime was 4.90% compared to 4.53%. For nine months they were 8.63% compared to 8.02% for the index. Even for the year they finally climbed ahead of that ugly first quarter of 1997 and were still better than the index by six basis points.

Changes made during the quarter included increasing their holdings of under one year by 5%, reducing 5-7 year holdings by 5%, and increasing in the 10-20 year. At the end of May they also shortened the portfolio, and they are currently at basically 100% of the index duration. They shortened duration for two reasons. One was that they saw some things happening in the market that lead them to believe that there might be some reversal of rates toward higher rates. It did happen, but now the rates have again fallen lower. The other reason was that they knew they were going to be asked to fund some upcoming equity investments.

Concerning sector breakdown during the quarter, Prime reduced U.S. Treasuries 4% and increased agencies. Since then they have reduced treasuries another 7% to 23%, increased finance another 1% to 34%, and increased industrial telephone holdings to about 10% (an increase of 5%). Thus, they have taken money out of treasuries these last two months and increased their holdings in finance and telephones. From the looks of the LBA, the corporates have continued to outperform the treasuries for the last month. Prime noted for the Board at its last meeting that the Asian problem (lower inflation and a moderately growing U. S. economy) would lead to even lower interest rates in 1998. They continue to feel that way, but recent market action causes some doubts about the timing and duration of this interest rate movement toward lower rates. So Prime has become more conservative in their maturity structure and reduced holdings of 20 year maturity U. S. Treasuries by 5%. That reduction reduced their portfolio duration to the duration of the index which at the end of May was 4.5 years. By Prime's preliminary figures, they are right on index duration for the portfolio.

The best portfolio Prime manages for PERF is an annuity savings account — the PERF Bond Fund. This is a portfolio that was put together 8-10 years ago at the direction of the PERF Board who indicated they wanted the portfolio to be a long bond fund with an average maturity of 15 years. That 15 year maturity averages out to about 178% of the duration of the LBA Index. The duration of the portfolio at the end of March was 8 years — the duration of the index was 4.49 years. This five year period has been a very good time to be long term oriented. This is a very conservatively run account. It is not treated actively, but money is invested when it comes in. When money is requested, it is sent and the 15 year average maturity is retained. In this portfolio Prime outperformed the index for one year by 4%, for two years it outperformed 1.4%, for three years 1.5%, for four years 90 basis points, and for five years 50 basis points.

With respect to Prime's contract with PERF, Mr. Tanner noted that some 14-15 years ago Prime was approached by the Board to manage fixed income money on a fixed fee basis rather than a basis point basis. When the money they managed went up, their fees did not increase proportionately. Thus, they ended up managing money at 1.5 basis points last year instead of 20. Now, with the reduction to their portfolio for investments in equities, their basis points will need to be increased from 1.5 to 3. Mark Webb informed Mr. Tanner that the Board had decided to continue all current contracts for six months from June 30, 1998. At that point there will be a reevaluation of each of the contracts to insure that the roles people have settled into over the years actually correspond with what the contract has them doing, and this matter would be a part of contract discussion at that time.

#### 4. REPORT ON PROGRESS OF BROAD AGENCY ANNOUNCEMENT

With respect to the search for mid-cap managers, Mr. Webb reported that the Broad Agency Announcement (“BAA”) left the PERF offices last week. The process of handling BAA’s has changed slightly in that the Department of Administration (“DOA”) uses a computer program different than that used by PERF. Thus, they have requested that they be given a hard copy of the BAA along with another copy on diskette which they will format to their specifications. The only thing left for PERF to do is to get a list to DOA of those firms who have requested their name be included for receipt of the BAA. It will be put out on the Internet and placed in *Pensions and Investments* magazine. It was Mr. Webb’s expectation that the BAA would be mailed by the end of the week. Following that, firms will be allowed to direct questions, in writing, to DOA , and DOA will forward those questions to PERF. PERF will then respond to DOA with written responses to each of the questions, followed by DOA responding directly to the interested parties. That done, a deadline will be established for receipt of the BAA by DOA.

Mr. Webb added further that it has taken quite a bit of time to finalize contracts from the last money manager search. That was due in large part to the fact that the State’s contract and the Board’s Investment Policy were not included as part of the BAA. They have been included this time. It has been stated in the BAA that the successful bidders will be asked to enter into these contracts and abide by the Board’s guidelines. “The staff went through a lot during the last search with individuals simply not understanding the statutory constraints the State is under and the environment in which they contract. The inclusion of the State contract and the Investment Policy will help expedite this process.”

5. RECESS

With no further business, the Board recessed to reconvene at 8:30 on June 2.



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Pete Keliuotis, William M. Mercer Investment Consulting  
Karen Franklin, National City Bank  
Faith Berning, National City Bank  
Susan Ruhl, Banc One  
Bruce Glor, Banc One  
Doug Todd, McCready & Keene, Inc.  
Don Hilt, PERF Retiree  
Mark Webb, PERF Interim Director  
Patrick Lane, PERF Executive Assistant to the Director  
Bill Hutchinson, PERF Division Director, Pension Administration  
Michael Quigley, Program Director, Pension Administration  
Dave Yeater, PERF Controller  
Tom Parker, Director, 1977 Police Officers' & Firefighters' Pension & Disability Fund  
Linda Petro, Recording Secretary

## 1. ACTUARIAL REPORT

Doug Todd was present representing McCready & Keene.

Mr. Todd's report began with a review of an experience study for the 1977 Police Officers' & Firefighters' Pension and Disability Fund. When this plan was implemented in 1977, an arbitrary employer contribution rate of 21% was established and has remained at that level over the last 20 years. The individual assumption of 6% did not, however, seem to measure up as well. That was one of the reasons an experience study was felt necessary. Additionally, there is a new Indiana statute which improves the benefits for the 1977 Police & Fire Fund by lowering the retirement age and also adding a number of liabilities by moving converted benefit recipients over into the 1977 plan. Thus, it became crucial to make sure that the plan is going to remain well funded.

The study covers the four years of January 1, 1993 through December 31, 1996. It compares current assumptions and, in some cases, the possibility of changing assumptions. The study does not review any assumptions in the old plans (pre-1977 plans). Those plans are not quite as crucial because the benefits are paid as they become due.

Following review of the assumptions for the 1977 plan, they were tested by running them with the January 1, 1997 valuation. The January 1997 valuation did not recognize the new statute for lowering the retirement age and moving the converted benefit recipients from the responsibility of the cities and town and into the 1977 plan. Cities and towns will continue to pay benefits through the end of September; however, after that they will be paid through the 1977 Fund. When the assumption changes were made and ran against the 1977 actuarial valuation, an employer contribution rate of 17.4% of first class salaries was determined as compared to the original 21%. Despite that result, McCready continues to recommend that the employer contribution rate remain at 21% based upon the fact that the 1977 valuation did not include the new police and fire statute. Also, the 1977 Fund has always been funded very conservatively. One of the main items of conservatism has been the retirement age. There has always been a 100% assumption on retirement age once an individual becomes eligible. That was done because the 1977 Fund, perhaps, was over funded, but the old plans (unfunded plans) had to be considered.

Following Board discussion,

**MOTION** duly made by Nancy Turner, seconded by Teresa Ghilarducci and unanimously carried to approve a 21% employer contribution rate for the 1977 Police & Fire Fund.

Mr. Todd continued that with the new statute, the retirement age is lowered from 55 to 52 with no reduction in benefits. An individual who so chooses could retire as early as age 50 with a benefit reduction to be determined by the Board. Following discussion of proposed actuarial reductions,

**MOTION** duly made by Teresa Ghilarducci, seconded by Nancy Turner and unanimously carried to adopt a simple 7% per year reduction for early retirement benefits in the 1977 Police & Fire Fund.

Finally, Mr. Todd explained that the old police and fire plans were established as pay-as-you-go plans. The new plan is funded by 21% from the employers and 6% from the employees. Thus, Indiana cities and towns are actually paying for two generations of police officers and firefighters — they are paying the existing benefits for the old plans, and they are prefunding the new plan. That is a significant load on the cities and towns. To help, the Pension Relief Fund was established and is funded from cigarette and alcohol taxes and lottery monies. That money is distributed to the cities and towns in two checks, one on June 30 and the other on September 30. It has been Board practice to approve distribution of those monies. Thus,

**MOTION** duly made by Steve Miller, seconded by Nancy Turner and unanimously carried to grant the Interim Director authority to approve various cities' and towns' Pension Relief distribution amounts (pursuant to the incorporated formulas), make such distributions, and communicate the rates to the cities and towns.

## 2. ANNUITY SAVINGS ACCOUNT DISCUSSION

Mary Beth Braitman, Ice Miller Donadio & Ryan, began the discussion by noting there were two items for Board action today. The first is to establish an interest crediting rate for the year ending June 30, 1998. This will be the last interest crediting rate established in an era when people had very little effective investment direction available to them. For the year ending June 30, 1997, the legislature established an interest crediting rate of 9%. The Investment Committee has felt it would be appropriate to continue that 9% rate for this last year. Mr. Miller added that given what happened last year and the fact that the Fund has had a pretty good year, 9% was an appropriate rate.

**MOTION** duly made by Steve Miller, seconded by Dwayne Isaacs and unanimously carried to approve a 9% interest crediting rate for the period ending June 30, 1998.

Secondly, unlike previous years when rates were established retrospectively, the second item for Board action would be to establish an interest crediting rate prospectively for the year ending June 30, 1999. The reasons being that there is a huge communication effort being undertaken by PERF staff, and they feel this would allow members to make a judgment/decision about their options in a

far more understandable way. Overriding concerns of members include safety of the account, preservation of capital, reasonable stability on interest rates, reasonable competitiveness of interest rates (compared to available "safe" rates), and a need for a positive interest rate (never zero). Staff feels that a very responsible formula would be one which would start with a very stable base (e.g. actuarial interest rate) and add to that percentage of a slow moving weighted average return (using indexes, not actual rate of return). With those thoughts in mind, the Investment Committee has recommended that for the year ended June 30, 1999, the interest crediting rate should be the actuarial interest rate plus 1%. Their key rationale was that this rate is significantly higher than any fixed income risk-free return available, and it is based on the expected long-term earnings potential of the total PERF portfolio with that 1% acknowledging the current positive economic conditions. Chairman Doermer added that what the Board would be doing would be to rely on the long term bias of the equities market to continue to rise. There will be years when it won't, but the long-term pattern is up, and that should serve the Fund as a whole rather well. Following further discussion,

**MOTION** duly made by Steve Miller, seconded by Dwayne Isaacs and unanimously carried to set the interest crediting rate on the Guaranteed Fund for the 1998-1999 fiscal year at the actuarial rate plus 1%.

Ms. Braitman continued that there was also a series of items which require Board action with respect to the annuity savings accounts. The first such item involved the structure of the options themselves.

#### ! Bond Fund

PERF staff has recommended that the Board choose one fixed income manager for this member direction. Because the underlying theme going into the new year is to give the participants the exposure to the asset classes that they need as well as to keep it as administratively simple as possible, it was the Investment Committee's recommendation that the Board use the LBA Index manager for the Bond Fund.

**MOTION** duly made by Teresa Ghilarducci, seconded by Nancy Turner and unanimously carried to accept the Investment Committee's recommendation to use one fixed income manager (the LBA Index manager) for the Annuity Savings Account Bond Fund.

#### ! Money Market

PERF staff feels that this will not be an attractive fund going forward. The Investment Committee's recommendation is that if there is some sort of an existing cash sweep fund post unitization of all the other accounts, and if it makes sense administratively to use that for the Money Market Fund, staff

should proceed accordingly, making sure an appropriate service fee is assessed.

**MOTION** duly made by Teresa Ghilarducci, seconded by Nancy Turner and unanimously carried to accept the Investment Committee's recommendation as so noted for the Money Market Fund.

! S&P 500 Index

PERF staff has recommended the use of one indexed large cap fund for this member direction. Those would be integrated dollars, since there is no reason to segregate employer and employee money in this fund. Both staff and the Investment Committee have recommended the use of Barclays Global Investors as the S&P 500 Index Fund manager.

**MOTION** duly made by Dwayne Isaacs, seconded by Steve Miller and unanimously carried to utilize Barclays Global Investors as the S&P 500 Index manager.

! Small Cap Fund

PERF staff has recommended the use of one small cap fund for this member direction. The Investment Committee has recommended the use of Dimensional Fund Advisors as the manager.

**MOTION** duly made by Steve Miller, seconded by Dwayne Isaacs and unanimously carried to use Dimensional Fund Advisors as the vehicle for the Small Cap Fund.

! Guaranteed Fund

The Board has already previously indicated that they wanted the Guaranteed Fund run with the total portfolio. Staff is currently working with National City Bank as to how that is going to fit in the unit trust structure. No Board action was required on this matter.

With respect to member fees, there is a statutory provision that provides that all administrative costs of each alternative program (everything but the Guaranteed Fund) shall be paid from the earnings on that program. The Board needs to consider whether to charge management fees or just produce a net rate of return for each option. Mr. Yeater, PERF Controller, noted that current policy on the Bond and Money Market Funds is to charge an annual fee of 10 basis points for administrative costs incurred by the Fund in order to maintain those records, etc. The investment management fees charged by the money managers have been absorbed by PERF. For a number of years, a fee of 60 basis points was used for administrative costs, but approximately two years ago the Fund began utilizing 10 basis points because it was felt that represented more fairly the

expense to the members who participated. Mr. Miller suggested that it might be appropriate for each fund to charge a two-component fee, one which covers the investment management fees and the other which covers PERF's administrative costs. Following further discussion,

**MOTION** duly made by Steve Miller, seconded by Dwayne Isaacs and unanimously carried to establish a two-part fee structure on the annuity savings account options comprised of the first part being the reimbursement of the investment management fees and the second part being an additional fee of five basis points per year (to vary in the future based on experience) for recovery of the PERF administrative costs.

Finally, Ms. Braitman noted that the Benefits Committee, at its meeting on June 1, recommended that the PERF staff continue working with William M. Mercer Investment Consulting on investment educational materials. There was a Benefits Committee/PERF staff recommendation that there be three additional staff positions created initially to deal with the annuity savings account activity (handle phone calls, questions about the election forms, distribution of materials, etc.). Three additional people is the minimum PERF staff feels they need to enable the Fund to get through this transition period. Hopefully, they would then be cross trained later. This level of staffing would keep the Fund well under the benchmarking results previously discussed and would also leave the Fund far below the 1997 survey of State and Local Governmental Employee Retirement Systems which shows that for systems with more than 100,000 active members, the average number of staff per 1,000 active members is 1.1. Applying that ratio to PERF, it would translate to approximately 165 staff members. The Benefits Committee has recommended that PERF staff work with Doug Kinser (Executive Assistant to the Governor) and Diana Hamilton (Special Liaison to the Governor for Public Finance) to facilitate the additional staffing discussed as appropriate and timely.

### 3. REPORT ON PROGRESS OF UNIT TRUST ACCOUNTING SYSTEM

The Board met on May 18 to adopt a resolution which directed PERF to work with Bank One and National City Bank to move the securities held by Bank One to National City Bank for record purposes in preparation of the implementation of the unit trust accounting and the new sub-custodian agreements entered into by National City Bank and Bank One. It was agreed between members of PERF, National City Bank, and Bank One that it would be a good idea to have both banks represented at today's meeting to give the Board a firm understanding of the status of the transfer of those assets.

Thus, Karen Franklin and Faith Berning were present representing National City Bank and Susan Ruhl and Bruce Glor were present representing Bank One. Ms. Franklin reported that the direct link from Bank One has been established, and National City's Cleveland office has experienced training on how to use the system. Bank One will be available for questions should there be any problems;

however, as of this date National City is custodian for all PERF assets and is instructing trades through Bank One with Bank One acting as the securities lending agent. Mark Webb added that all the contractual agreements have been signed and are in effect. By July 1, PERF will be a unitized fund. Mr. Webb added further that the State Board of Accounts has been intricately involved in the process and essentially gave their blessings as to the manner in which this has evolved.

#### 4. ADMINISTRATIVE MATTERS

##### Marcia Hess Reinstatement of Service Issue

IC 5-10.3-7-15 Sec. 15. reads:

A persons who has fifteen (15) or more years of creditable service in the fund and has withdrawn from the fund before reaching the age of sixty-five (65) years may apply for reinstatement of eligibility, if the person:

- (1) makes the application before July 1, 1998, and within ninety (90) days after reaching the age of sixty-five (65) years; and
- (2) demonstrates that further employment with an employer covered by the fund is impractical due to health or other conditions as determined by the board.

The board has the ultimate authority whether to grant reinstatements of eligibility.

Bill Hutchinson, PERF Division Director of Pension Administration, informed the Board that PERF had now received an application for reinstatement under this statute. The individual, Marcia Hess, left her position with the State in December of 1989. She, at that point, was vested with PERF in terms of her years of service but had not yet reached an appropriate retirement age. She could have resigned her PERF-covered position and left her monies in PERF, and at age 60 she would have qualified for full retirement benefits. However, she filed for a refund of her employee contributions and in so doing forfeited everything. Typically, in situations of this nature an individual will find work in another PERF-covered position for six months and then have their service reinstated. This lady is physically unable to do that, and the statute allows her to petition for reinstatement in the Fund without working the six months. Such reinstatement would entitle her to a defined benefit only in that she has already withdrawn her employee contributions.

**MOTION** duly made by Teresa Ghilarducci, seconded by Nancy Turner and unanimously carried to accept Marcia Hess' application for reinstatement of service.

### Building Manager Update

Patrick Lane, PERF Executive Assistant to the Director, reported on the operational expenses of the two buildings owned by PERF (143 West Market Street and 125 West Market Street). As of two months ago, the Department of Revenue, housed at 143 West Market Street, was approximately \$16,000 in arrears on rent due to some confusion as to the manner in which payment should be made. The Data Processing Oversight Commission, housed at the 125 West Market Street building, was also in arrears on their rent in the amount of \$31,000. Half of that amount has now been paid.

The 125 building is totally occupied, and the 143 building is about 85% occupied. That 15% vacancy is due to the fact that the seventh floor is currently unused. Plans are to utilize that space to expand the PERF offices, but nothing can be designed with respect to the work space until a full grasp of staffing issues has evolved out of the Coopers & Lybrand report.

### Quarterly Financial Update

Dave Yeater reported that the Fund still has more money budgeted than is being spent. However, some of that excess will be depleted in the areas such as postage and printing due to mailings necessitated to educate members with respect to the new annuity savings account options. Also, there continues to be an over expenditure in the area of staffing due to the need to hire temporary employees.

Chairman Doermer inquired concerning the budget for office equipment. Mr. Yeater reported that there was a two-year allotment of \$1.5 million for equipment, of which \$1.2 was allotted for document imaging.

### New Units & Enlargements

**MOTION** duly made by Teresa Ghilarducci, seconded by Steve Miller and unanimously carried to approve the following new units and enlargements:

#### New Units

1682 - West Township

#### Enlargements

448 - Franklin Community Schools  
558 - School City of Whiting  
639-001 - LaPorte County Solid Waste District  
644 - Logansport Community School Corp.  
776 - City of Richmond  
846 - Tri-Creek School Corporation



859	-	Monroe Central School Corporation
881	-	Taylor Community School Corporation
978	-	Goshen Community Schools
995-001	-	South Henry Regional Waste District
1017	-	Putnam County
1027	-	Town of Lowell
1049	-	Salem Community Schools
1091	-	Maconaquah School Corporation
1097	-	MSD Pike Township
1107-001	-	Adams County Solid Waste Management District
1156	-	Speedway Public Library
1169	-	Southeastern Career Center
1189	-	Town of Markle
1199	-	Marion-Adams Schools
1224-001	-	Brown County Solid Waste Management
1228	-	Eckhart Public Library
1233	-	Town of St. John
1262	-	MSD of Wayne Township
1404	-	Franklin County Community School Corp.
1451	-	Clinton Public Library
1471	-	Decatur County
1475	-	Hancock County
1476	-	Town of Millersburg
1479	-	Town of Milan
1484	-	Salem Public Library
1511	-	Jackson County Public Library
1545	-	Town of Odon
1560	-	Whitley County Consolidated Schools
1566	-	Town of Westport
1611	-	Ripley County
1617	-	Town of Poseyville
1620	-	Town of Dayton
1626	-	Town of New Harmony
1669	-	Town of Whiteland
1673	-	Town of Crothersville

### Legal Update

Mark Webb reported that there are three primary outstanding law suits, all of which involve non-PERF funds. Two of those suits involve police and fire with respect to baseline standards for performing the duties of a police officer and firefighter which an individual has to pass to be admitted to the 1977 Fund. Two individuals, each one for reasons of profound hearing loss, have been unable to pass the standards related to hearing and, therefore, were not certified by the local board. PERF is being defended in those cases by the Attorney General's Office. Irrespective of what happens, PERF has no legal liability in these cases.

The other suit involves a former legislator. This is an issue regarding the 1989 creation of the Legislators' Defined Contribution System. In the 1989 session, the Legislature decided that its pension system needed improvements and overhaul, and, thus, a new plan was created. It was determined at that time that all of those legislators who were serving as of a certain date would be eligible to be included in the new system. Those who had completed their service prior to that set date would remain in the old plan. This class action suit was initiated by a former legislator who completed service in the 1970's and felt he should be afforded the same benefit as those included in the new system. Motion for summary judgment has been filed in this case, and PERF is simply awaiting a ruling.

Mr. Webb also noted that the Fund received word in April that they were facing a potential law suit to be brought by Conservation & Excise over the calculation of benefits. It is the belief of both Mr. Webb and Mary Beth Braitman that the only way a change can be implemented is through legislation. Therefore, PERF has written back with an explanation that for reasons set forth in statute, the retirement rates cannot be raised as requested. Hopefully, that will be enough to dissuade anything further coming of this.

## 5. BUREAU OF MOTOR VEHICLES

Mrs. Braitman reported concerning the Bureau of Motor Vehicles Commission's ("BMVC") desire to participate in PERF. She noted that BMVC elected to go with a defined contribution plan ten years ago and is now coming back to the defined benefit plan.

They are very unhappy with their defined contribution plan in that the performance did not turn out to be all it was supposed to be in terms of investments, the administrative costs turned out to be far more than they were supposed to be, and all in all it has not been a good experience for the Bureau. Thus, they would like to come back to the defined benefit structure, and PERF is a very good structure for them to look at. Their Board has not made a final decision, but it looks as though all recommendations from their staff will be to go into PERF. If that is the case, they would be seeking the PERF Board's approval, at the November meeting, as an enlargement of the State.

Ms. Braitman and Mark Webb have been meeting with the Commission to determine how to most readily complete such a move. McCready and Keene will be doing a lot of work with respect to costing. It will take some degree of staff time on PERF's part and a lot of staff time on the part of BMVC, but if successfully completed, it will be a very interesting testimonial to the PERF benefits. Ms. Hamilton added that it would also be a very strong statement of confidence in PERF by people who obviously have an option to do something different since by State statute they can set up whatever plan they would like for their employees.

Mr. Miller inquired as to who absorbs all the costs with the actuarial and legal time involved. Mr. Webb responded that each fund would pay their own legal fees. According to McCready & Keene calculations, there would still be an annual additional \$250,000 expense to the State to absorb these employees in the plan, and it will increase the employer contribution rate.

6. OTHER BUSINESS

Tom Parker, Director of the 1977 Police & Fire Fund, noted that pursuant to statute, members of the Police & Fire Fund are awarded an annual cost-of-living adjustment to be determined by the Board. The adjustment is the average January, February, and March year-to-year comparison of the Consumer Price Index and has been calculated as 1.4% for the current year. Following discussion,

**MOTION** duly made by Teresa Ghilarducci, seconded by Steve Miller and unanimously carried to adopt a 1.4% cost-of-living adjustment for members of the 1977 Police & Fire Fund and converttees to that plan.

7. NEXT MEETING DATE

By common consent, meetings for the remainder of calendar year 1998 were set as follows:

August 27 and 28  
November 30 and December 1

8. BOARD VACANCY

Chairman Doermer advised the Board of the fact that Dwayne Isaacs would be leaving his position as Trustee.

We know how blessed we've been with you and how respectful we are of your good judgment and your background and your contributions to the thinking of this Board at a very critical time in it's life, and we are very grateful to you, Dwayne. We've had the services of a very, very competent guy, and we appreciate you very much.

9. ADJOURNMENT

There being no further business, a Motion to adjourn was entertained, and by unanimous vote, the meeting was adjourned.

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Richard T. Doermer  
Chairman

Mark C. Webb  
Interim Director